Majesco

Fiscal 2018 First Quarter Conference Call

July 26, 2017

CORPORATE PARTICIPANTS

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CONFERENCE CALL PARTICIPANTS

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PRESENTATION

Operator:

Good day, everyone and welcome to the Majesco Fiscal 2018 First Quarter Conference Call. Today's conference is being recorded.

At this time, I would like to turn the conference over to Andrew Berger. Please go ahead, sir.

Andrew Berger:

Thanks, Rebecca and good afternoon to you all. A complete disclosure of our results can be found in our press release that was issued this afternoon. As a reminder, today's call is being recorded, and a replay will be available on our website shortly after the conclusion of this call.

During today's call, we will make statements related to our business, that may be considered forward-looking under Federal Securities Laws. These statements reflect our views only as of today and should not be reflected upon as representing our views as of any subsequent date. We disclaim any obligation to update any forward-looking statements or outlook. These statements are subject to a variety of risks and uncertainties that could cause actual results to differ materially from expectations.

At times, in our prepared comments and in responses to your questions, we may offer incremental metrics to provide greater insight into the dynamics of our business or our quarterly results. Please be advised that this additional detail may be one time in nature and we may or may not provide an update in the future. Also during the course of today's call, we will refer to certain non-GAAP financial measures. A reconciliation schedule showing GAAP versus non-GAAP results has been provided in our press release that was issued today after the market closed.

Hosting the call today are Ketan Mehta, Majesco's CEO and Co-Founder, Farid Kazani, CFO and Treasurer, and Ann Massey, Senior Vice President of Finance.

At this time, I will turn the call over to Ketan. Ketan?

Ketan Mehta:

Thank you, Andy. Good afternoon, everyone and welcome to Majesco's fiscal 2018 first quarter conference call. Over the last few quarters, we have been talking about Majesco's transition and growing our cloud-based operating model. We made significant progress in our cloud journey during this quarter. Total revenue from the cloud business for the first quarter grew 23% over the same quarter of the previous year. In addition, annualized recurring revenue for the cloud business grew 56% over the same quarter of the previous year.

As I've shared before, in October of last year, we signed a partnership deal with IBM, where IBM selected Majesco's platform as a part of their strategic imperative to offer industry platform solution, combining Majesco's core platform with IBM Watson and Internet of Things capabilities, offered on IBM Cloud, which insurance carriers can consume on pay-as-you-grow model. I'm very excited to share that we have signed a 10-year cloud subscription deal with IBM to support insurance clients. This is one of the largest deals for Majesco, with a potential value of over $35 million for cloud subscription component only.

We are excited about the future industry and customer impact of our IBM partnership, and I'm very encouraged by the progress our combined teams have made in the marketplace. I look forward to sharing more about this engagement as the relationship develops.

When we engage with the existing and potential insurance customers, they are all cognizant of the generational transformation underway, not only impacting how they think about insurance, but also how they interact with their customers. A rapidly growing digital age is underway. New competitors, new business models and new products are being launched in the market in a fraction of time and cost. The appetite for traditional multi-year, multi-million dollar, on-premise custom configuration is waning. In this new age of insurance, the focus is on speed to value, and Majesco is extremely well positioned to benefit on this emerging trend.

As a result of these changes, Majesco's transition from a primarily and on-premise business model to a growing cloud-based operating model will continue throughout fiscal 2018. I'm happy to announce that during the quarter, we had four clients successfully go into production, six customers expand their implementation into new states for new products and one insurer successfully upgraded their billing systems, which is a matter of great pride and accomplishment for our clients and us.

In addition to IBM, American Capital Assurance Corp., headquartered in St. Petersburg, Florida, offering commercial property insurance on admitted basis has selected Majesco's suite of P&C, inclusive of Policy, Billing, Claims and Rating, Majesco Distribution Management, Majesco Business Analytics and Majesco Enterprise Data Warehouse to transition from an outsourced provider.

During the last quarter earning call, I mentioned that we will experience revenue growth from quarter two of this fiscal. The revenue performance during the quarter is of $27.9 million. It's in line with our expectations. Strong order book closures during the quarter resulted in a significant uptick in the 12-month order backlog, which increased by 21% to $77.2 million from $64 million at the end of the previous quarter. This signal's a positive growth momentum in revenue for the rest of the year.

Margins for the quarter have been negatively impacted, primarily due to decline in revenue and in ramp up of cost to support our expected revenue growth in coming quarters. I'm also pleased to share that Homesite Insurance, a tier one customer was recently selected as a Novarica Impact Award winner for the Digital Initiative category. Homesite Insurance launched a sales portal with Majesco CloudInsurer using Majesco Policy for P&C and Majesco Billing core systems. The initiative was completed in little over a year, supports product bundling, delivered up to 40% premium cost savings to customers, and enabled expansion for other lines of business to support their growth strategy.

This recognition was selected by members of Novarica Insurance Technology Research Council, a knowledge-sharing group of hundreds of insurance CIOs. The recognition further raises the profile of Majesco CloudInsurer and digital offerings in the market.

To conclude, there is a fundamental market shift taking place in the industry, where carriers are looking for low investment risks, pay-as-you-grow and speed-to-value business platforms to position them for growth in the new insurance digital age. The platform provides an ability to innovate new products, reach new markets, create new customer experiences and liberate new and different business models for a new generation of customer.

We have growing list of real-life case studies, enabling our clients to innovate, grow and transform their business models through our CloudInsurer platform as a new start-up or a Greenfield backed by existing insurers or backed by venture capital, as well as traditional insurers. As we continue to ride this shift, we expect to build a strong cloud business with a high-margin recurring revenue business. With that, let me turn the call over to Farid, to discuss the financial drivers for the quarter.

Farid Kazan:

Thank you, Ketan and good afternoon to all, and welcome to our first quarter conference call. Fiscal 2018 will continue to be a year of transition, with the business model moving towards the cloud-based solutions. While it may not be completely visible in this quarter or the revenue profile for the fiscal 2018, the primary deal momentum on cloud-based business will develop into a higher recurring revenue base, translating to an improved profitability model.

Let me now share the specific numbers for the first quarter fiscal 2018. Revenue for the first quarter ended June 30, 2017 was $27.9 million, as compared to $32.6 million in the corresponding quarter of the last year, down 14.2%. The revenue for the quarter was—has been in line with our expectations, and has seen the stabilization of the revenue compared to the decline that has been witnessed by the Company over the last four quarters. For the quarter ended June 30, 2017, gross margins were at $11.9 million, which is 42.6% of the revenue as compared to $14.7 million, which is 45.3% in the quarter ended June 30, 2016. The drop in the margins has been primarily due to the decline in the revenue and the ramp up of the resources to support the revenue growth in the coming quarters.

The R&D expenditure for the fiscal 2018 first quarter was $3.93 million, which is 14.1% of the first quarter revenue, as compared to $4.5 million, which is 13.9% of the revenue during the same period of fiscal 2017. The decline in the R&D expenses has been primarily due to the lower cost, post consolidation of our Policy Admin platform. The SG&A expense for the first quarter fiscal 2018 was $10.3 million, which is 36.9% of revenue, as compared to $10.7 million, which is 32.7% of the revenue during the first quarter of fiscal 2017. The increased percentage of the SG&A was primarily due to the planned expenses of the sales and marketing effort.

The net loss for the first quarter ended June 30, 2017 was $1.7 million, or a loss of $0.05 per share as compared to a net loss of $0.6 million, or a loss of $0.02 per share for the same period of fiscal 2017. The Adjusted EBITDA for the first quarter ended June 30, 2017 was negative $0.4 million as compared to $1 million during the quarter ended June 30, 2016.

From a geographic standpoint, the North America, the U.K. and the APAC regions represented 89.7%, 5.3% and 5% respectively, of the first quarter's total revenue as compared to 89.3%, 7.3% and 3.4%, respectively, for the same period of the last fiscal 2017.

In terms of business split, the P&C business represented 80.5%, the Life and Annuity represented 17.5% and the rest was non-insurance business, for the first quarter of fiscal 2018. As compared to 79.8%, 18.4% and the rest from the non-insurance, respectively, from the corresponding period last year. With the change in revenue profile, the Company will provide certain metrics, specific to the cloud business starting the current quarter. The total number of cloud customers stood at 31, up from 29 customers at the end of same quarter in the previous year.

The total cloud income consists of the cloud recurring and the cloud implementation revenue. The annualized recurring revenue from cloud business grew 56% to $10.2 million in the quarter one of fiscal 2018, as compared to $6.4 million in the quarter one of fiscal 2017. The total revenue from the cloud business, which includes recurring and implementation, grew 23% to $7.4 million, which is 26.5% of the total Q1 revenue over $6 million, which was 18.4% of the total revenue for the same period of fiscal 2017. This total recurring revenue, which includes license revenues, recurring cloud subscription and maintenance and support, increased to 26.5% of the total income in the first quarter fiscal 2018, as compared to 22% in the fiscal—of the first—fiscal first quarter or for the first quarter of the last fiscal.

We will continue to share the above metrics going forward and over a period of time, share other relevant metrics with maturity and growth of our cloud business.

In terms of client concentration, the top customer in the fiscal first quarter represented 6.1%, while the top five constituted 24% and the top 10 constituted 40.4%. Majesco's 12-month order backlog at the end of June 30, 2017 was $77.2 million as compared to $64 million at the end of March 31, 2017 and $63.4 million at the end of June 30, 2016.

Quickly turning on to the balance sheet. Majesco had a cash and cash equivalent of $10.3 million as at 30 June, 2017, as compared to $14.9 million at the end of June 30, 2016 and 12.5%—$12.5 million as at 31 March, 2017. The total debt as at June 30, 2017 stood at $17.7 million, compared to the same number $17.7 million at the end of June 30, 2016 and $12.6 million at the end of March 31, 2017.

DSOs stood at 82 days at the end of June 30, 2017 as compared to 67 days in the previous quarter ended 31 March 2017. While this is higher than the normal operational level, it's due to a specific clear aberration, and will get normalized during the second quarter. Headcount was 2,279 at the end of June 30, 2017 as compared to 2,192 at the end of March 31, 2017.

This concludes our prepared remarks. I'll now pass it onto the Operator to please open the call for questions. Thank you very much.

Operator:

Thank you. Ladies and gentlemen, the question-and-answer session will be conducted electronically. If you would like to ask a question today, you may do so by pressing star, one on your telephone keypad. If you are using your speakerphone, please release your mute function before pressing the corresponding digits. Once again that is star, one to ask a question.

Your first question will come from Brian Kintslinger with Maxim Group.

Josh Seide:

Hi, guys. This is Josh Seide in for Brian. Thanks for taking the questions. Firstly, regarding the IBM subscription deal announced today, should we essentially think of this as a support and maintenance arrangement with IBM to support clients that purchase Majesco's cloud solutions through its partnership with IBM? Is that kind of the right way to think about that deal?

Ketan Mehta:

Hi, Josh. Let me understand your question. It is—the deal covers the cloud subscription for the use of the platform and that's our primarily revenue stream in addition to other services as well as possibly maintenance and support. The 35 million potential number, which I mentioned is primarily for the cloud subscription part of it.

Josh Seide:

Okay. I think I understand that. It's—essentially, it's a cloud subscription in support of the IBM subscription arrangement that was previously announced? Is that correct?

Ketan Mehta:

That is correct.

Josh Seide:

Okay. Can you give us a sense, kind of qualitatively of the Company's pipeline in terms of the deal size and customer size, and how that has been evolving given the ongoing partnership with IBM?

Ketan Mehta:

I'm feeling very good about the growing pipeline, the—both with Majesco direct sales team as well as our combined pipeline with IBM partnership. The nature of the partnership primarily comes from a variety of carriers. With IBM, there are larger tier clients in the pipeline. In Majesco pipeline, it is across the board. We have some Greenfield initiatives of the large insurance carriers, some start-up carriers as well as some established traditional carriers as well.

Josh Seide:

Just jumping back to the IBM partnership, is that essentially—will IBM essentially be re-selling Majesco's cloud solutions, kind of in a white-label fashion through its network?

Ketan Mehta:

No, the way to look at it is that, this is part of the IBM industry platform initiatives. IBM launched a vertical industry platform where Majesco's core platform will be part of it. As I mentioned earlier, it will also include some of the Watson capabilities, as well as Internet of Things capabilities and other solutions that IBM will integrate as a part of their overall industry platform solutions.

Josh Seide:

Okay, and then just quickly on the P&L. You mentioned, based on the solid bookings this quarter, you expect revenue growth for the remainder of the year, is that correct? Is that on a year-over-year or sequential basis?

Farid Kazan:

Josh, can you just repeat that?

Josh Seide:

I'm sorry?

Farid Kazan:

Yes. Can you just repeat the question?

Josh Seide:

Sure. I think I recall that on the call, you mentioned the solid bookings position in the Company for revenue growth throughout '18. Is that on a year-over-year or sequential basis?

Farid Kazan:

On a sequential basis.

Josh Seide:

Lastly, should we expect gross margins to kind of come down in the near-term as they did this quarter to kind of position the Company to support accelerated growth in coming quarters?

Farid Kazan:

Josh, so the gross margins were down because of the ramp-up of the costs that we are doing for the growth, including the project on IBM. We do expect the revenues from these businesses to ramp up from the first month in July of this quarter. Which is why some of the costs that had to be taken in this previous quarter ended June, and that is why we've had a good amount of impact, negative impact in this June quarter. Hopefully, we would see margins to play out much better, because we would have revenues from those particular projects that are ramping up.

Josh Seide:

Understood. Thank you.

Operator:

From Antithetos Capital, Mike Chadwick.

Mike Chadwick:

Yes. Hi, gentlemen. I think I'm new to your calls here. I wanted to congratulate you on this IBM announcement to start.

Ketan Mehta:

Thank you.

Mike Chadwick:

Sure. I just—I wanted to kind of just go back to the—basically the headcount. It just sounded like you may have increased headcount sequentially by about 90 employees. Does that sound about right?

Ketan Mehta:

That is correct. That's right.

Mike Chadwick:

Okay. For me, what I'm trying to do is, I typically look at companies in terms of software and software-as-a-service model, right? We try and extrapolate best practices and looking at sort of what are typical revenue per employee metrics and other things. When I go back and look at the last trailing 12-months, we get about a $117 million revenue run rate, but you've got 22,179 employees. When we look at that, that puts us right around $51,500 per employee roughly. Okay, back of the envelope type math. I think one of the things that we need to think about in terms of the Company going forward is, as you were transitioning from a software to a software-as-a-service model, it's like an American baseball game, there's nine innings.

If you look at the revenue in the last few quarters, you've sequentially been down, I think four quarters in a row, roughly about $1 million a quarter, give or take a little bit. That's probably—I know you're forecasting sequential revenue growth. But the truth is, is when we move to a software-as-a-service model, there's a lot of cannibalization, because of the amortization of the revenue model. Here's my point. My point is, is that if you look at most software companies—excuse me, software-as-a service companies that are publicly traded, that are some of the leaders out there in the field, the starting point, sort of the poker chips on the table, is more of about a $200,000 revenue per employee metric to really get the gross margins to a level that actually can help scale the business and get to the profitability metrics we've got.

I just wanted to kind of throw that out there, and then at the same time get your opinion on that, in terms of how we might more closely resemble that type of model perhaps down the road in the future?

Ketan Mehta:

Yes, at this point of time, the cloud recurring revenues is roughly around 9.1% of the total quarter's—first quarter's fiscal revenue. While we are ramped up to kind of build for the business on the cloud platform, what you are going to see is that once it starts maturing, after the implementation on this cloud business happens, you will see the subscription revenue that we start building up pretty aggressively, okay? Which will, in the end not only better the revenue per employee, but also will help better the entire gross margins for the business.

At this point of time, we have not scaled to the level, which is reflecting the metrics that you talked about. But over a period of time, as the business starts building up, you will see the benefit of the subscriptions revenue kind of giving advantage in terms of the overall metrics shaping up much more positively.

Mike Chadwick:

Understood, and I guess for me, when I saw that headcount increase, I was a little surprised and maybe taken back by that. Maybe if you can kind of point to and give us some color as to why you felt you needed increased headcount given where we're at already?

Farid Kazan:

The headcount increase has happened across the geographies in the U.S. and in Asia-Pac, okay? There has been headcount increase in the requirement for our sales and marketing engines. In order to kind of support the revenue growth, which is both from the cloud business and the rest of the business, which we are expecting, we needed to kind of ramp up that cost. Yes.

Mike Chadwick:

Okay, and then—and clearly that flows through to the bottom line, right, because we—in terms of sort of our Adjusted EBITDA model at this point. Having said that—right. When these transitions occur, as I alluded to that metaphor of an American baseball game, it's a long and sort of winding road regardless of how much business we're booking, right, the idea that we're recognizing revenue over one, two, three-year agreements, it takes a lot of time to recognize that revenue. My point in this is that, we might be in the second or third inning perhaps in this ball game, but it's going to take quite a bit of time for that offset of the cannibalization from the traditional lumpy software license revenue to the SaaS or subscription process. If that's the case, I read a press release that went out in India.

I don't think it came out here in the U.S., and it talked to the idea that the organization is currently considering potentially a dividend to shareholders at the upcoming Annual Meeting. I'm just asking, if I can—if you can provide us a little bit more insight as to the thinking about that, given we're at a point in time where we've got margins that are coming down and we're not at profitability. Help me understand the thinking behind that?

Farid Kazan:

It's basically the parent company, okay, which has—it's primarily, the business which is related to India and based on the performance of that independent parent company, okay? The Board of Directors are proposing a kind of the first maiden dividend for the shareholders out there. Okay? While we do expect that the support from the parent is there for the business in the U.S., but clearly, the parent company has that profitability and cash availability to kind of reward the shareholders at the parent level with some dividends. But again, it's a decision by the Board. The Board Meeting is expected shortly and they will take a decision accordingly.

Mike Chadwick:

Are you suggesting that if a dividend was initiated in India, that it would not affect the U.S. entity and/or the cash on the books here? Is that what you are saying?

Farid Kazan:

No, it will not, because I don't think it's going to be a dividend that is going to—in whatever little dividend that gets announced at the parent level for the small shareholders out there is going to impact the business out here. It will not.

Mike Chadwick:

Okay. Because I mean if we were—I mean, while I may be a minority shareholder in this situation, what I would say is that, if it was to impact our cash that is down sequentially here quarter-to-quarter, I would not be in favor of that as a minority shareholder.

Farid Kazan:

No. If you look at the Majesco U.S. consolidated entity, it is self-sufficient in terms of the cash requirement, and it has enough cash to kind of manage its own operations. It has a potential to kind of improve the cash flow going forward on its own. At this point of time, it doesn't even have to depend on the parent for any cash flow requirement.

Ketan Mehta:

Yes, and I think I'll just clarify that the parent is an independent entity, which has 70%—which owns 70% of the U.S. Company. But this dividend will, in no way impact the U.S. Company's financials or cash positions.

It's primarily out of the cash available with regards to the parent company.

Mike Chadwick:

Right. Okay. There you clarified that. I appreciate that. That helps, and again, congratulations on the significant extension of the IBM agreement.

Ketan Mehta:

All right. Thank you.

Farid Kazan:

Thank you.

Operator:

As a reminder everyone, that is star, one to ask a question. There appears to be no other questions at this time.

Andrew Berger:

Thanks, Rebecca. We'll talk to you, when we report Q2 in the next several months. Thank you.

Ketan Mehta:

Thank you.

Operator:

Ladies and gentlemen, that does conclude today's presentation. We do thank everyone for your participation.